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UNCLAS SECTION 01 OF 02 HARARE 002820

SIPDIS

STATE FOR AF/S
NSC FOR SENIOR AFRICA DIRECTOR JFRAZER
USDOC FOR 2037 DIEMOND
PASS USTR ROSA WHITAKER
TREASURY FOR ED BARBER AND C WILKINSON
DEPARTMENT PASS USAID FOR MARJORIE COPSON

¶E. O. 12958: N/A
TAGS: ECON EPET EFIN ETRD ZI
SUBJECT: Keeping the Lights On in Zimbabwe

¶1. Summary: The GoZ will need to spend over twice its revenue to meet appropriation goals in 2003, according to our calculations. It will react to this bleak predicament by printing money, enduring shortages and relinquishing national assets. End Summary.

¶2. In spite of its veneer of transparency, the GoZ does not disclose foreign exchange transactions. This is quite an omission, since they now comprise most GoZ spending. We integrated domestic and foreign accounts into the following matrix for 2003, converting the domestic transactions into U.S. dollars at the present parallel rate of Z$ 1580:1:

EXPENDITURES

a. Critical :

Food Imports	$ 140,000,000
Fuel Imports	$ 330,000,000
Energy Imports	$ 110,000,000
Civil Service Salaries	$ 169,000,000
Critical Infrastructure	$ 26,000,000
Total Critical Expenditures	$ 775,000,000

b. Ordinary:

Other External Payments	$ 426,000,000
Budgeted Expenditures	$ 293,000,000
Total Ordinary Expenditures	$ 719,000,000
Total Expenditures	$1,494,000,000

REVENUE

Foreign Exchange Inflows	$ 350,000,000
Tax Revenues	$ 342,000,000
Privatizations	$ 13,000,000
Total Revenue	$ 705,000,000
SHORTFALL	$ (789,000,000)

¶3. A few notes on our methodology:

a.) We accepted GoZ estimates for domestic expenditure and revenue at face value, although past years have shown that overruns are common.

b) For foreign accounts, we relied on industry estimates as well as an internal Reserve Bank working paper of Oct 4.

c) Due to the high political cost of reductions, we counted civil service salaries and benefits as a critical expenditure.

d) Critical infrastructure includes what it costs to keep air traffic, police, power stations, etc., in operation.

e) Forex inflows mostly reflect GoZ expectations from a 40 percent withholding of export earnings, which is subsequently exchanged at the official rate (3 percent of market value). After increasing the withholding to 50-100 percent in the 2003 budget, the Government now forecasts that revenue will grow while most economists believe it will move in the other direction. We left earlier projections unchanged.

f) "Critical" levels of fuel and energy cited above probably reflect over-consumption at controlled or subsidized prices. Fuel is often purchased at Zimbabwe service stations solely for resale abroad. If the GoZ allows these subsidized prices to rise toward market-determined levels, demand will fall.

Comment

¶4. This is a very grim picture. Still, the many variables make it extremely difficult to develop a model that demonstrates what Zimbabwe must spend each day or month to forestall economic meltdown. The GoZ will have to make a number of unpleasant decisions during 2003.

¶5. We do not see any way the GoZ could begin again to service external debt next year, in spite of Finance Minister Murerwa's budget statements that Zimbabwe "cannot continue to default on [its] external debt commitments . . . [and the Government is] determined to initiate a credible program to reduce these arrears." We expect the GoZ to expand money supply aggressively and spend substantially less on food, fuel and energy imports that it would like. Although shedding more public assets in garage-sale fashion would be a blow to national pride, perhaps even more so than an orderly privatization with foreign bidders, the GoZ may decide that this is the only way to stave off unbearable shortages. The GoZ has already reportedly exchanged assets with Libya for oil, and the internal Reserve Bank document suggests the GoZ may need to lease or sell Air Zimbabwe's planes as a potential source of revenue. (An executive from a U.S. ground support equipment supplier believes equity in Air Zimbabwe's 2 767s and 3 737s would be worth US$ 260 million in the open market.) Perhaps the GoZ's only consolation may be that even subsidized energy consumption should fall in an economy that is deindustrializing.

Sullivan